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No.

SUPREME COURT, U.S.
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1986

LEONARD BRAWER,

Petitioner,

vs.

THE OPTIONS CLEARING CORPORATION and AMERICAN STOCK EXCHANGE, INC.,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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QUESTIONS PRESENTED FOR REVIEW

When a securities exchange and its clearing house violate their own rules, rules required by a statute that protects investors even in the absence of fraud:

1. Does an investor who is injured by the violation have a claim under the statute?

2. If he has such a claim must he make a showing of fraud or bad faith in order to maintain it?

3. Does he make a sufficient showing of fraud or bad faith to defeat a motion to dismiss where the court finds it a troublesome and close question whether the defendants' conduct was in good faith?

PARTIES TO THE ACTION

Petitioner Leonard Brawer is an individual investor who was injured by the conduct of the respondents.

Respondent The Options Clearing Corporation ("OCC") is a Delaware corporation and is a registered clearing agency under § 17A of the Securities Exchange Act of 1934 (the "Act"). Respondent American Stock Exchange Inc. is a New York corporation and is a registered national securities exchange under § 6 of the Act. Each respondent is a self-regulatory organization ("SRO") under §§ 3(a)(26) and 19(g)(1) of the Act. A-5, 17.

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LEONARD BRAWER,

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PETITION FOR A WRIT OF CERTIORARI TO
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In this action to recover damages against a securities exchange and its clearing house for violating their own rules, under §§ 6(b), 17A(b)(3), and 19(g)(1) of the Securities Exchange Act of 1934, petitioner Leonard Brawer, plaintiff-appellant below, prays this court for a writ of certiorari to review the judgment of the Second

Circuit entered December 11, 1986 and the order of the Southern District of New York dated April 29, 1986.

OPINIONS BELOW

The opinions of the Second Circuit (A-1) and of the Southern District of New York (A-15) are reported, respectively, at 807 F.2d 297 and 633 F. Supp. 1254.

STATEMENT OF JURISDICTIONAL GROUNDS

The judgment of the Second Circuit (A-54-55) was dated and entered December 11, 1986. By order of January 9, 1987 the Second Circuit allowed the late filing of a petition for rehearing. (A-56). By order of February 11, 1987, the Second Circuit denied the petition for rehearing. (A-57-58). The jurisdiction of this court is invoked under 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS AND RULES INVOLVED

The relevant provisions of the

statutes and rules involved are reproduced in the appendix. Section 6(b), 15 U.S.C. § 78f(b), is at A-50-51, as it was originally, and at A-3, as it has been since the Securities Acts Amendments of 1975 (the "1975 Amendments"). Section 17A(b)(3), 15 U.S.C. § 78q-1(b)(3), is at A-3-4. Section 19(g)(1), 15 U.S.C. § 78s(g)(1) is at A-4. Section 11 of article VI of the bylaws of OCC is at A-49-50. Rules 902 and 903 of the Rules of the Board of Governors of the Annex are at A-48-49.

STATEMENT OF THE CASE

On Friday, March 1, 1985, petitioner Brawer was holding short positions in listed put options on the stock of Phillips Petroleum Company ("Phillips"). These options were traded at the market of respondent Amex and cleared by respondent OCC.

Before March 1, Phillips had proposed a refinancing plan which it denominated a recapitalization, and the Amex and OCC had announced that the Phillips options would be adjusted if the stockholders approved the plan. However, the plan failed to win approval. Next, over the March 1, 1985 weekend, Phillips proposed a second plan that would have an even greater effect on its capital structure, but both plans had an extraordinarily substantial effect. Before the recapitalization, Phillips had a debt equity ratio of one to three. The first plan would have turned it around to three to one. The second plan changed it to four to one. The second plan succeeded, but the Amex and OCC failed to adjust. A-5-9. Their sole reason given was that the second plan was actually an exchange offer for which

no adjustment was required, rather than a recapitalization for which it was. A-8.

Adjustments are required as provided in OCC bylaws, article 6, §11. See A-49-50. The purpose of the adjustment rules is the protection of investors. They are, in substance, an expanded form of anti dilution rule as is found in convertible bond indentures and the instruments governing stock purchase warrants and convertible preferred (or common) stock. Anti dilution provisions are designed to protect persons who invest in warrants and convertibles. Without them there is no protection. The American Bar Foundation, Commentaries on Indentures, at p. 527 (1971) explains it succinctly:

> The anti-dilution provisions are designed to preserve the value of the conversion privilege against

diminution by certain voluntary corporate acts. For example, if the conversion price is $25 a share at a time when the common stock has a market value of $30 a share, the conversion right is clearly valuable. If the Company should then split its stock 3 for 1, the market price of its shares would be reduced to approximately $10 per share. Thus the value of the right to convert at $25 per share would have been virtually destroyed, by that voluntary corporate action, in the absence of appropriate protective provisions.

Inasmuch as ownership of a convertible debenture does not give the holder the rights of a shareholder, the holder of a convertible debenture would have almost no protection against acts by the Company which would adversely affect the value of the common stock issuable on conversion, such as a split-up of shares, stock dividends, distribution of assets, issuance or sale of other convertible securities, issuance of options, issuance or sale of common stock at prices below the current conversion or market price, merger, sale of assets or dissolution and liquidation of the Company. Events of this type are customarily described as "diluting" the value of the conversion privilege, and if protection is desired against such dilution, appropriate provisions must be included in the indenture.

[Footnote omitted]

The major difference between the anti dilution provisions just described and the adjustment rule for listed options is that the former seek to protect the holder of what is, in substance, a call, and the latter seeks, by its terms, to protect the writers as well as the holders and as to puts as well as calls.

Brawer was damaged because the recapitalization would cause a decline in the market price of Phillips stock, as Phillips had said. In anticipation of the decline in the price of the stock, the price of the puts rose, and since Brawer was short puts he lost. This technical description should not obscure the fact that what Brawer had done, in substance, was to agree to buy Phillips stock, at the option of the seller, at a fixed

price. As a result of the recapitalization and the SROs' failure to adjust, he became burdened with the duty to buy stock which had become diluted, but he had to pay the same price as if no dilution had occurred. I have estimated such damage to the entire short put class as approximately $15 million.

Brawer sued under §§ 6(b), 17A(b)-(3), and 19(g)(1) of the Securities Exchange Act of 1934, 15 U.S.C. §§ 78a et seq. (the "Act"), relying principally on Baird v. Franklin, 141 F.2d 238 (2nd Cir.) cert. denied 323 U.S. 737 (1944) for the rule that an implied claim exists and that it is governed by a negligence standard.

The jurisdiction of the District Court rested on § 27 of the Act, 15 U.S.C. § 78aa. The jurisdiction of the Second Circuit rested upon 28

U.S.C. § 1291.

The defendants below answered the complaint and served motions to dismiss. The grounds for these motions were that there was no private right of action under the Act to redress the wrongs alleged in the complaint and that such an action could not be maintained without a showing that the defendants had acted fraudulently or in bad faith. In their moving papers the defendants stated that they had not acted fraudulently or in bad faith. In order to test these assertions, the district court allowed the plaintiff to take two depositions limited to the bad faith issue.

The District Court dismissed the complaint on the grounds that no private right of action existed. It held that the action previously allowed by Baird v. Franklin had not been

preserved in the 1975 Amendments. It did not reach the fraud issue.

The Second Circuit expressly declined to rule upon the issues that served as the basis for dismissal by the District Court. Instead, it affirmed on the grounds that the action could not be maintained in the absence of allegations of fraud or bad faith and that Brawer had failed to make a sufficient showing of either.

In the course of its opinion the Second Circuit held that the conduct of the Amex and OCC raised "troublesome" and "close" questions on the issue of bad faith. A-14. Accordingly, Brawer filed a petition for rehearing with a suggestion for rehearing in banc. The Second Circuit denied the petition for rehearing without an opinion.

REASONS FOR GRANTING THE WRIT

This is a case against the most powerful and sophisticated professionals in the securities industry, i.e., the exchanges, clearing houses, and other such groups defined by statute as self regulatory organizations ("SROs"). When SROs act they have the capacity to do great harm. Without the protections provided by the federal securities laws and particularly the provisions involved here, SROs are private clubs run for their own benefit and wholly unaccountable to investors. That such private club status is simply intolerable has been recognized by nearly everyone, and it has been a mainstay of public policy, as embodied in the Securities Exchange Act, for more than fifty years. The necessary function of SROs in the process of capital formation, allocation, and

liquidity is too important to allow them to return to those days of immunity and privilege.

The decisions below have introduced substantial, live conflict upon the question of the standard of conduct required of SROs and, even worse, upon the very question whether an investor is entitled to any relief at all.

There is much public concern these days over the fairness of the conduct of participants in the securities industry, some of whom have lately been found to have acted in cynical disregard of the law and with contempt for the rights of investors. The questions presented in this case go to the heart of that public concern in that they will determine whether and by what standards investors can secure their federal statutory protec-

tions against SROs. In short, this action questions the fairness of the market itself which, as is seen here, is driven not by an invisible hand but by self interested people. Their self interest caused them to be uninformed about important facts and careless in making a decision affecting the investors that the law requires them to protect. As a result of the decisions of the courts below these lords of the market are unaccountable to those very investors.

I

THIS COURT SHOULD GRANT THE WRIT TO RESOLVE CONFLICTS CONCERNING WHETHER AN INVESTOR HAS AN IMPLIED CLAIM AGAINST AN SRO THAT VIOLATES ITS OWN RULES.

This court has never expressed an opinion on Baird v. Franklin, which is the leading case that supports the petitioner's claim. As the District Court noted, it was followed pretty

much by all courts. (A-24-26). In reference to Baird the Ninth Circuit in Hughes v. Dempsey-Tegeler & Co., Inc., 534 F.2d 156, 167 (9th Cir.) cert. denied 429 U.S. 896 (1976), held:

> [Judge Clark's] opinion is recognized as the dispositive analysis of the Exchange's duty and breach of duty under Section 6.

As the Second Circuit noted, there is conflict on the question whether Baird v. Franklin, supra, "remains good law after the 1975 Amendments to the Act and recent Supreme Court decisions." (A-5). In addition to the references of the Second Circuit, there are two other cases worth noting. The Ninth Circuit, addressing the effect of two decisions of this court, Cort v. Ash, 422 U.S. 66 (1975) and Securities Investor Protection Corp. v. Barbour, 421 U.S. 412 (1975), held

that nothing in these cases "mandate[s] a reversal of the longstanding rule that a private action is available under Section 6." Hughes v. Dempsey-Tegeler & Co., Inc., supra, 534 F.2d at 166 n.5. The Third Circuit has disagreed with the Ninth Circuit. See Walck v. American Stock Exchange, Inc., 687 F.2d 778 (3rd Cir. 1982) cert, denied, 461 U.S. 942 (1983).

I submit that Baird v. Franklin was preserved by Congress in the 1975 Amendments. Merrill Lynch, Pierce, Fenner, & Smith, Inc. v. Curran, 456 U.S. 353 (1982). Although the Second Circuit noted that courts were in conflict upon this question, it did not resolve the conflict. (A-5). The Curran rule is applicable here because Congress noted the existence of Baird v. Franklin with approval as it conducted its investigations

which resulted in the 1975 Amendments. See p. 27 n.21 of the Securities Industry Study Report of the Subcommittee on Securities of the Committee on Banking, Housing and Urban Affairs of the United States Senate, 93rd Cong., 1st Sess. (Committee Print 1973) (the "Securities Industry Study"). Congress declined to enact legislation nullifying Baird v. Franklin, but it did nullify two decisions of the Judicial Panel on Multidistrict Litigation which had ordered pretrial transfer and consolidation, pursuant to 28 U.S.C. § 1407, of SEC enforcement actions with private civil actions. Senate Committee on Banking, Housing and Urban Affairs, S. Rep. No. 75, 94th Cong., 1st Sess. at pp. 73-77, reprinted in 1975 U.S. Code Cong. & Ad. News 179 ("Senate Report"). Congress also expressly stated its

intention to clarify the decision in Rosenfeld v. Black, 445 F.2d 1337 (2nd Cir. 1971). Senate Report at p. 71. Conversely, Congress never said that it wanted even to change, much less abolish, Baird v. Franklin.

The 1975 Amendments codify the principle of Baird v. Franklin and make no change in the statute insofar as it supports Baird. The principle established in Baird v. Franklin is that, since the statute requires a securities exchange to have rules, the exchange must comply with and enforce those rules. Otherwise, the statute would have no purpose.

In its old and new forms §6 requires that a national securities exchange have rules. The reason that Congress changed §6 was to make it clear that exchange rules be capable of protecting investors. See new §6(b)(5). Congress

had expressed some doubt that this was required by old §6. Senate Report at p. 27. The new statute, §6(b)(1), adds that a securities exchange must be able "to comply ... with ... the rules of the exchange," and §19(g)(1) also expressly requires exchanges and, indeed, all SROs to comply with their own rules.

Even without the Curran rule, the petitioner's claim is maintainable under Cort v. Ash, 422 U.S. 66 (1975), as Judge Clark's opinion in Baird v. Franklin is entirely consistent with Cort v. Ash, as at least one court has noted. Rich v. New York Stock Exchange, Inc., 509 F. Supp. 87, 88-89 (S.D.N.Y. 1981). As previously noted, the Ninth Circuit and the Third Circuit have disagreed with each other on this question.

Even before reaching the Second

Circuit's basis for decision this court is presented with conflicting lower court decisions concerning the meaning of a new statute that regulates a substantial and significant industry. In the many years since Baird v. Franklin was decided this court has never ruled upon it, but the lower federal courts followed it almost without exception. Now, however, the lower courts are responding to mixed signals from this court which have, unfortunately, resulted in a lack of clear authority, and they are producing conflicting decisions over the fundamental issue whether an investor even has a claim at all. Accordingly, this court should resolve the conflict.

II

THIS COURT SHOULD GRANT THE WRIT TO RESOLVE CONFLICTS CONCERNING WHETHER AN INVESTOR MUST SHOW FRAUD OR BAD FAITH TO RECOVER ON AN IMPLIED CLAIM AGAINST AN SRO THAT VIOLATES ITS OWN RULES.

A. The Limitations on Discretion Imposed by § 6 Preclude a Fraud or Bad Faith Standard.

The origin of the negligence standard, rather than a fraud standard, is Baird v. Franklin, where the court limited the discretion of securities exchanges not to obey and enforce their own rules and held, 141 F.2d at 244:

> If all that §6(b) meant was that every exchange should pass token regulations, incapable of enforcement except at the wish of the exchange itself, there would have been no purpose for its inclusion in the Act. Sections 6(b) and (d) were surely intended to be read together, and the latter makes it clear that the purpose of the requirements of the former is "to insure fair dealing and to protect investors." This can be realized only if §6(b) is construed as imposing the twofold duty upon an exchange of enacting certain rules and regulations and of seeing that they are enforced.

On the question whether fraud or bad faith must be alleged the Ninth Circuit has held that it need not. Instead, in Hughes v. Dempsey-Tegeler & Co., Inc., supra, 534 F.2d at 170, the court imposed a standard of reasonableness, contingent upon prompt action, taking into account all the facts and circumstances. Reasonableness, I submit, is essentially the same as a negligence standard. The court also held, 534 F.2d at 167:

> "Standing alone, the fact that the Exchange acted in good faith is not a sufficient defense against an action brought under Section 6."

The court was concerned lest a securities exchange be given too much discretion in the matter of enforcing its rules. In any event, if good faith is not a defense, it is unnecessary to allege bad faith.

I submit that this limitation

on discretion was undisturbed by the 1975 Amendments because they only strengthened the protection of investors.

The Second Circuit cited Schonholtz v. American Stock Exchange, Inc., 376 F. Supp. 1089, 1092 (S.D.N.Y.) aff'd. 505 F.2d 699 (2nd Cir. 1974) as authority for imposition of a fraud standard. A-11. There the district court cited Colonial Realty Corp. v. Bache & Co., 358 F.2d 178 (2nd Cir.) cert. denied, 385 U.S. 817 (1966) and Buttrey v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 410 F.2d 135 (7th Cir) cert. denied 396 U.S. 838 (1969). These cases impose a fraud standard, but they are expressly and specifically limited to actions against member firms rather than securities exchanges, a distinction the court carefully drew in Colonial. When

the court affirmed Schonholtz it did so on the grounds that no Baird v. Franklin claim could exist "when no rules were violated." 505 F.2d at 700. The court in Schonholtz did not reach the fraud issue in §6 claims.

Although, as the Second Circuit noted, cases against commodities exchanges have imposed a fraud standard, A-10-11, I submit that cases against commodities exchanges are unreliable as precedent for a fraud standard here. The cases under the Securities Exchange Act have consistently rejected a fraud standard. Congress enacted 7 U.S.C. § 25(b)(4) for the express purpose of imposing a fraud standard in cases against commodities exchanges. Even though this merely codified existing law, Congress was well aware of Baird v. Franklin, its limitations on discretion, and its negligence

standard for liability, but it never enacted a fraud standard for liability of securities exchanges as it did for commodities exchanges.

I am not aware of any authoritative explanation of the difference in the standard of civil liability of securities exchanges and commodities exchanges. I submit that there is nothing unfair in the negligence or reasonableness standard and that there is no compelling reason to drive securities investors into the posture of commodities investors, especially where Congress itself has not done so.

A negligence standard is fair when SROs make an erroneous decision as to whether to adjust. It is their market which they have undertaken to manage. They or their members profit from it. Options trading is a significant part of the Amex's busi-

ness, and options clearing is the only business of OCC. The adjustment rule is their rule, and, as Congress believed, investors have the right to rely on proper compliance with that rule. Securities Industry Study, p. 5 (acknowledging "the reliance placed by public investors on the operation of the self-regulatory agencies").

The position of the SROs in this case is substantially similar to that of a depositary in escrow in that both hold other peoples' money for the purpose of delivering it to the right person. The courts treat depositaries in escrow as fiduciaries and impose upon them nearly absolute liability for failure to make a proper delivery or payout. 20 (Revised) N.Y. Jur., Escrows §§ 6, 25. I submit that it is fair to apply the same

principles to the SROs.

No one has taken issue with the proposition that the SROs' decision not to adjust was clear error. Courts have consistently held that a recapitalization occurs when a corporation makes and carries out an exchange offer of new bonds for old stock. Microdot, Inc. v. United States, 728 F.2d 593 (2nd Cir. 1984); Comm. v. Neustadt's Trust, 131 F.2d 528 (2nd Cir. 1942); see Wood v. Coastal States Gas Corp., 401 A.2d 932, 940 (Del. 1979) (a spinoff distinguished from an exchange). No one has taken issue with the proposition that the failure to adjust resulted in the misallocation of approximately $15 million.

I submit that to allow such whimsical, capricious, and disastrous action by SROs strips investors of the protections of the Act. It is no answer

that it simply "benefit[s] one group of option investors at the expense of another." A-12. The chance to win an undeserved windfall is not the protection contemplated by the Act. In such circumstances, the denial of judicial review except for fraud does not reduce market uncertainty, A-12, but merely substitutes one kind of uncertainty, a less acceptable kind I submit, for another.

B. The Limitations on Discretion Imposed by § 17A Preclude a Fraud or Bad Faith Standard.

Section 17A was added to the Act by the 1975 Amendments. Previously, clearing houses such as OCC were regulated as subsidiaries of exchanges. Moreover, although clearing agencies sometimes operate independently of exchanges, OCC is unique and does nothing but clear options and for nobody but the members of the securities

exchanges that trade options. See Securities Exchange Act Rel. No. 20221 (Sept. 23, 1983) 28 SEC Docket 1175, 1196-98. These options exchanges could not function without the OCC, and it is no different from a securities exchange in this regard. See Daniel v. Board of Trade, 164 F.2d 815, 817 (7th Cir. 1947).

Section 17A repeatedly insists upon "prompt" but also "accurate clearance and settlement of securities transactions." Congress declared this to be "necessary for the protection of investors." §17A(a)(1)(A). It also provides that clearing houses must have "the capacity" ... for "prompt and accurate clearance," §17A-(b)(3)(A), and that their rules must be designed to promote it. §17A(b)-(3)(F).

The adjustment rule falls within

regulation by §17A. It is a significant part of the clearing of options trades, because it can change the securities which are deliverable upon exercise of the option.

Congressional concern with accurate clearing means that the adjustment rule must be accurately applied. And whatever discretion SROs might have to interpret some of their own rules as they see fit, in this case such interpretations must yield to the statutory command of accuracy. In other words, an interpretation of the adjustment rule that is not accurate does not meet the statutory requirement. To the extent that the adjustment rule provides for discretion, that discretion is limited by the statutory requirement of accuracy.

The substance of the SROs' adjustment decision in this case exhibits

a distinct lack of comformity to statutory standards. Adjustment was required if Phillips had undergone a recapitalization. I submit that what Phillips did produced a sufficient "reshuffling of a capital structure, within the framework of an existing corporation," Helvering v. Southwest Consol. Corp., 315 U.S. 194, 202 (1942), to constitute a recapitalization. And the method by which this reshuffling was accomplished, i.e., an exchange offer rather than a vote of the stockholders, does not change it. See pp. 25-26, supra.

I submit that the requirement of accuracy cannot be satisfied by mere honesty. It would have been surprising if Congress had said that honesty alone would suffice and had required clearance and settlement merely to be free of fraud or bad faith. The purpose of §17A was to

cure the problems in the late 1960's that prevented "prompt and accurate clearance and settlement of securities transactions." These problems have almost universally been assigned to technical failures rather than fraud. See Senate Report at p. 4, which said:

> The "paperwork crisis" of the late 1960's resulted from the securities and banking industries inability to process the tremendous volume of trading that swept all securities markets. All too often deliveries to customers of both cash and securities were late and stock certificates were lost in the rising tide of paper. Securities firms lost control of their records and over 100 brokerage firms were forced into liquidation -- largely as a result of faulty recordkeeping and backlogs of uncompleted transactions. These liquidations caused financial hardships to many investors who left their securities with brokerage houses for safekeeping. One economic historian recently characterized this crisis as "perhaps the single most dramatic technical failure of the free-enterprise system on record anywhere."

As this case demonstrates, clearing errors can result from causes other

than faulty recordkeeping and backlogs, but there is no reason to tolerate inaccurate clearing whatever the cause. The Second Circuit's opinion does not address the issue of the requirement of accuracy under §17A of the Act.

III

EVEN IF FRAUD OR BAD FAITH IS REQUIRED, THE PETITIONER HAS MADE A SUFFICIENT SHOWING SO THAT DISMISSAL AT THIS STAGE IS IMPROPER.

I submit that where, as here, the court characterizes the question of fraud or bad faith as close and troublesome, then there is sufficient reason to sustain the complaint.

The close and troublesome question, as the Second Circuit held, A-14, was whether the Amex and OCC sterilized their discretion by waiting from early Monday, before trading began, until late Thursday, after it ended, to "decide" not to adjust. During this

period, their staff members had responded to investors' inquiries by stating that no adjustment would be made. This court held that the mere delay, "without more," did not constitute bad faith. Here, however, there was more -- the statements of the staff members that locked the SROs' committee into only one possible adjustment decision. A similar claim of sterilized discretion was held sufficient in Daniel v. Board of Trade, 164 F.2d 815, 818, 820 (7th Cir. 1947). In Daniel the court held that bad faith was sufficiently alleged upon pleading that the exchange adopted a particular rule

> for the added purpose of attempting to protect themselves against the possible liability which might be assessed against them by reason of the anti-trust action which had been brought by Cargill, Inc....

While the Second Circuit stated that

the delay was necessary to enable the committee to marshal information, the delay failed to accomplish this purpose. The record reveals a startling ignorance of the facts by the committee members. They failed to read the prospectus and to discuss the financial consequences, and this should raise more troublesome questions as to just how this decision was made and by whom. The decision to call the committee meeting was not made by OCC's chairman. He could not even say who called the meeting. Where, as here, the proof of how the decision was made is in the hands of the Amex and OCC, "dismissals prior to giving the plaintiff ample opportunity for discovery should be granted very sparingly." Hospital Building Co. v. Trustees of Rex Hospital, 425 U.S. 738, 746 (1976). Only two limited purpose

depositions have been taken, and nine people were present at the March 7 telephone meeting, including one more committee member.

The Second Circuit also overlooked the sharp dissimilarities between Brawer's claim that the adjustment decision benefited the Amex and OCC by generating increased trading volume and revenues and the assertion, in Sam Wong & Son, Inc. v. New York Mercantile Exchange, 735 F.2d 653, 672 (2nd Cir. 1984), that exchange members faced only a remote and theoretical possibility of detriment. In the instant case the fact of increased trading has been shown, and we have also submitted an affidavit of an options broker explaining the connection between the committee's decision and the increased trading. The court sustained allegations of fraud and bad faith

in Daniel v. Board of Trade, supra, upon a showing that I submit was no stronger. Here, following McLain v. Real Estate Board of New Orleans, Inc., 444 U.S. 232 (1980), and Hospital Building Co. v. Trustees of Rex Hospital, supra, Brawer should be permitted to attempt to show the connection between the SROs' adjustment decision and the substantial benefits that they actually reaped.

I submit that the Second Circuit went beyond the limited function of a federal court in deciding a motion to dismiss. In Scheuer v. Rhodes, 416 U.S. 232, 236 (1974) this court held:

> The issue is not whether a plaintiff will ultimately prevail but whether the claimant is entitled to offer evidence to support the claims. Indeed it may appear on the face of the pleadings that a recovery is very remote and unlikely but that is not the test. Moreover, it is well established that, in

> passing on a motion to dismiss, whether on the ground of lack of jurisdiction over the subject matter or for failure to state a cause of action, the allegations of the complaint should be construed favorably to the pleader.

Quoting from Conley v. Gibson, 355 U.S. 41, 45-46 (1957) this court recently held in McLain v. Real Estate Board of New Orleans, Inc., supra, 444 U.S. at 246:

> It is axiomatic that a complaint should not be dismissed unless "it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief."

I submit that the Second Circuit went too far in concluding, essentially, that there could be no set of facts that Brawer could present to show that the Amex and OCC sterilized their discretion or acted to benefit themselves by increased trading.

CONCLUSION

The petition for writ of certiorari

should be granted, and the judgments below should be reversed.

Respectfully submitted

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Dated: May 12, 1987

APPENDIX

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

No. 102—August Term, 1986

(Argued October 8, 1986

Decided December 11, 1986)

Docket No. 86-7416

LEONARD BRAWER,

Plaintiff-Appellant,

— against —

THE OPTIONS CLEARING CORPORATION and AMERICAN STOCK EXCHANGE, INC.,

Defendants-Appellees.

Before:

LUMBARD, CARDAMONE, and PIERCE,

Circuit Judges.

Appeal from a judgment entered in the Southern District of New York, Louis L. Stanton, Judge, dismissing

appellant's complaint alleging violations of the Securities Exchange Act of 1934, 15 U.S.C. §§ 78f(b), 78q-1(b)(3), and 78s(g)(1), for lack of a private right of action.

Affirmed.

A. ARNOLD GERSHON, P.C., New York, N.Y., *for Plaintiff-Appellant.*

ROGER PASCAL, Chicago, Illinois (Burton R. Rissman, Joseph H. Nesler, Schiff Hardin & Waite, Chicago, Illinois; M. William Munno, Sewart & Kissel, New York, N.Y., of counsel), *for Defendant-Appellee The Options Clearing Corporation.*

Lord, Day & Lord, New York, New York (Eugene F. Bannigan, Gordon L. Nash, Laurie E. Foster, Monica A. Derham, of counsel), *for Defendant-Appellee The American Stock Exchange, Inc.*

RICHARD A. KIRBY, Assistant General Counsel, Securities and Exchange Commission, Washington, D.C. (Paul Gonson, Solicitor, Daniel L. Goelzer, General Counsel, Jacob H. Stillman, Associate General Counsel, Leslie E. Smith and Katharine Gresham, Attorneys, Securities and Exchange Commission, Washington, D.C., of counsel), *as Amicus Curiae.*

LUMBARD, *Circuit Judge*:

Leonard Brawer appeals from a judgment dismissing his complaint against defendants The Options Clearing Corporation (OCC) and American Stock Exchange, Inc. (AMEX) entered in the Southern District by Judge Louis L. Stanton on April 29, 1986. Brawer's complaint alleges that OCC and AMEX violated §§ 6(b), 17A(b)(3), and 19(g)(1) of the Securities Exchange Act of 1934, as amended (the Act), 15 U.S.C. §§ 78f(b), 78q-1(b)(3), and 78s(g)(1) respectively,[1] by failing to comply with their

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[1]Sections 6(b)(1) and (5), 15 U.S.C. §§ 78f(b)(1) and (5), as amended, state:

> (b) An exchange shall not be registered as a national securities exchange unless the Commission determines that—
>
> (1) Such exchange is so organized and has the capacity to be able to carry out the purposes of this chapter and to comply, and (subject to any rule or order of the Commission pursuant to section 78q(d) or 78s(g)(2) of this title) to enforce compliance by its members and persons associated with its members, with the provisions of this chapter, the rules and regulations thereunder, and the rules of the exchange.
>
> (5) The rules of the exchange are designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest; and are not designed to permit unfair discrimination between customers, issuers, brokers, or dealers, or to regulate by virtue of any authority conferred by this chapter matters not related to the purposes of this chapter or the administration of the exchange.

In relevant part, §§ 17A(b)(3)(A), (F), and (G), 15 U.S.C. §§ 78q-1(b)(3)(A), (F), and (G) provide:

> (3) A clearing agency shall not be registered unless the Commission determines that—
>
> (A) Such clearing agency is so organized and has the capacity to be able to facilitate the prompt and accurate clearance and settlement of

own rules. The district court, in an opinion reported at 633 F. Supp. 1254, dismissed the complaint, concluding that Brawer lacked a private right of action. OCC and AMEX, in a joint brief, argue that the district court should be affirmed either on the ground stated in its opinion or on the alternative ground that Brawer failed to allege fraud or bad faith in his complaint. The Securities and Exchange Commission (SEC) also submits an amicus

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securities transactions for which it is responsible, to safeguard securities and funds in its custody or control or for which it is responsible, to comply with the provisions of this chapter and the rules and regulations thereunder, to enforce (subject to any rule or order of the Commission pursuant to section 78q(d) or 78s(g)(2) of this title) compliance by its participants with the rules of the clearing agency, and to carry out the purposes of this section.

(F) The rules of the clearing agency are designed to promote the prompt and accurate clearance and settlement of securities transactions, to assure the safeguarding of securities and funds which are in the custody or control of the clearing agency or for which it is responsible, to foster cooperation and coordination with persons engaged in the clearance and settlement of securities transactions, to remove impediments to and perfect the mechanism of a national system for the prompt and accurate clearance and settlement of securities transactions, and, in general, to protect investors and the public interest; and are not designed to permit unfair discrimination in the admission of participants or among participants in the use of the clearing agency, or to regulate by virtue of any authority conferred by this chapter matters not related to the purposes of this section or the administration of the clearing agency.

(G) The rules of the clearing agency provide that (subject to any rule or order of the Commission pursuant to section 78q(d) or 78s(q)(2) of this title) its participants shall be appropriately disciplined for violation of any provision of the rules of the clearing agency by expulsion, suspension, limitation of activities, functions, and operations, fine, censure, or any other fitting sanction.

The introductory paragraph of § 19(g)(1) of the Securities Exchange Act of 1934, 15 U.S.C. § 78s(g)(1) in relevant part, provides:

Every self-regulatory organization shall comply with the provisions of this chapter, the rules and regulations thereunder, and its own rules

. . . .

brief which urges affirmance on the latter ground. Agreeing with this position, we affirm and hold that a private cause of action against an exchange or a clearinghouse for failure to comply with one of its rules which requires an exercise of discretion, if one exists at all, may be brought only if it is premised upon allegations of fraud or bad faith.[2]

Brawer alleges the following: AMEX, a national securities exchange registered pursuant to § 6 of the Act, 15 U.S.C. § 78f, maintains a market for trading in stocks, bonds and options. All options listed on AMEX are cleared through OCC, a clearing agency registered under § 17A, 15 U.S.C. § 78q-1. Both AMEX and OCC are self-regulatory organizations (SROs) as defined by § 3(a)(26) of the Act, 15 U.S.C. § 78c(a)(26). Phillips Petroleum Company (Phillips), whose stock trades exclusively on the New York Stock Exchange, lists its options on AMEX.

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[2]Accordingly, we express no opinion on two issues argued by the parties on appeal. First, whether *Baird v. Franklin*, 141 F.2d 238 (2d Cir.), *cert. denied*, 323 U.S. 737 (1944), remains good law after the 1975 Amendments to the Act and recent Supreme Court decisions. *Compare Brawer v. Options Clearing Corp.*, 633 F. Supp. 1254 (S.D.N.Y. 1986) (*Baird* no longer remains good law), *with Rich v. New York Stock Exchange*, 509 F. Supp. 87 (E.D.N.Y. 1981) (holding that recent Supreme Court decisions do not eliminate the private cause of action established in *Baird* and arguing that the Congressional silence regarding *Baird* in the 1975 Amendments indicates approval of the then-existing private cause of action under § 6). Second, whether *Baird v. Franklin* may be extended after the 1975 Amendments to support a private cause of action for an SRO's failure to comply with its own rules. *Compare Brawer*, 633 F. Supp. at 1257 n.5 (no significant distinction between the facts of *Baird* and a case where an investor claims that an SRO failed to comply with its own rules) *and Bright v. Philadelphia-Baltimore-Washington Stock Exchange*, 327 F. Supp. 495 (E.D. Pa. 1971) (member stated cause of action against exchange by claiming that exchange had intentionally violated the election provisions of its constitution), *with Lenowitz v. Philadelphia Stock Exchange, Inc.*, 502 F. Supp. 428 (E.D. Pa. 1980) (finding *Bright* no longer persuasive in light of the evolution of the law since that decision).

Brawer sold—in securities parlance "wrote" or took a "short" position in—a number of puts in Phillips stock which were outstanding on March 1, 1985.

A "put option" obligates the seller (writer) to buy shares of the underlying security at a stated price (exercise price), if the buyer (holder) decides to exercise the option prior to its expiration date. Generally, one purchases a put option as insurance. A put option establishes a floor at which the holder will always be able to sell the underlying security; if the price drops below the option's stated exercise price, the holder will be able to invoke the option and sell the securities. On the other side, the option writer essentially takes on the downside risk in exchange for the price of the option. Therefore, if the price of the underlying security falls precipitously, as apparently happened to Phillips stock in this case, the writer may suffer a significant loss.

In December, 1984, a Texas partnership led by T. Boone Pickens, Jr. announced an unsolicited tender offer for Phillips stock. As a defensive tactic, Phillips' board of directors proposed a plan which included the exchange of its own debt securities for 38 per cent of its common stock, the sale of 32 million newly issued shares of common stock to an employee stock ownership plan, and the purchase of the Texas partnership's stock in Phillips at a premium. The price of Phillips stock fell substantially upon the announcement of the plan. The plan did not become effective, however, because it failed to receive the requisite number of votes at a special meeting of Phillips shareholders.

Shortly after this plan was proposed, another hostile bidder for Phillips emerged, led by Carl Icahn of New York. Between the close of business on Friday, March 1,

and the opening of trading on Monday, March 4, Phillips fashioned and announced a second financing scheme. Under this second plan, Phillips would issue a package of debt securities for half of its outstanding common stock. In its offer to purchase, Phillips noted that the likely effect of its offer would be to drive down the price of its common stock. The second hostile bidder withdrew its tender offer in response to this plan.

Both AMEX and OCC have procedures for adjusting option prices in response to changes in the market for an underlying security. AMEX rules 902 and 903[3] make options being traded on AMEX subject to adjustment in accordance with OCC rules. Article VI, Section 11(d) of OCC's Bylaws[4] provides that in the case of a

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[3]Amex Rules 902(a) and 903(c) and (d) provide:

Rule 902.

(a) Subject to the provisions of Rules 905, 907 and 909, the rights and obligations of holders and writers of option contracts of any class of options dealt in on the Exchange shall be as set forth in the rules of the Options Clearing Corporation.

Rule 903. * * *

(c) The unit of trading and the exercise price initially established for option contracts of a particular series are subject to adjustment in accordance with the rules of the Options Clearing Corporation. When such adjustment or adjustments have been determined, announcement thereof shall be made by the Exchange and, effective as of the time specified in such announcement, the adjusted unit of trading and the adjusted exercise price shall be applicable with respect to all subsequent transactions in such series of options.

(d) Option contracts shall be subject to adjustments in accordance with the rules of the Options Clearing Corporation.

[4]OCC By-laws, Article VI, § 11(d) states:

In the case of any reorganization, recapitalization, reclassification or similar event with respect to shares of underlying securities for which adjustment is not provided in any of the foregoing paragraphs of this Section 11, or in the case of any event for which adjustment

"reorganization, recapitalization, reclassification or similar event" affecting the underlying security, "the Securities Committee shall make such adjustments in the exercise price, trading unit or number of contracts . . . as that Committee in its sole discretion determines to be fair to the holders and writers of such option contracts."

Although OCC and AMEX had indicated that they would adjust if the first plan became effective, they made no adjustment in response to the second plan. Nor did they halt trading after the announcement of the second financing plan. When trading opened on Monday, March 4, 1985, the prices of Phillips options rose immediately and steeply as the market responded to expectations of a decline in price of Phillips stock when the plan was implemented. During the following week, OCC and AMEX received numerous telephone calls asking whether they would adjust Phillips options prices in response to the second financing plan. Both OCC and AMEX indicated that no adjustments were likely. The OCC Securities Committee, consisting of two officers of AMEX and the chairman of OCC, held a telephone meeting on Thursday, March 7, 1985, at 3:30 in the afternoon, to discuss the question. They decided that the transaction should be classified as an exchange offer,[5] and, in accordance with longstanding

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is provided in one of the foregoing paragraphs but is not considered by the Securities Committee to be appropriate under the circumstances, the Securities Committee shall make such adjustments in the exercise price, trading unit or number of contracts with respect to the option contracts affected by such event as that Committee in its sole discretion determines to be fair to the holders and writers of such option contracts.

[5]The parties disagree as to whether the second financing scheme should be designated a "recapitalization" or an "exchange offer." Under the view we take, we need not consider this disagreement.

policy, decided not to adjust prices in response. This decision was announced prior to trading on Friday, March 8. Brawer alleges that the Securities Committee took this action because they believed that unadjusted Phillips options would be more useful as instruments of arbitrage, thereby increasing trading volume and the revenues of the exchanges.

In an effort to recover his losses, Brawer commenced this action on behalf of himself and all other writers of Phillips puts who had options outstanding on March 1, 1985. OCC and AMEX moved to dismiss the complaint on two grounds. First, they claimed that the Act does not create a private cause of action for the failure of an exchange or a clearing house to comply with its own rules. Second, they argued that, even if a cause of action existed, a claim that OCC and AMEX failed to comply with their respective adjustment rules could stand only if the complaint alleged bad faith or fraud. The district court granted the motion on the first ground and dismissed the complaint, concluding that the Supreme Court's recent reluctance to imply causes of action under federal statutes, combined with the changes made by the 1975 Amendments, had undermined *Baird v. Franklin*, 141 F.2d 238 (2d Cir.), *cert. denied*, 323 U.S. 737 (1944), and eliminated the private right of action for violations of these three sections.[6] Consequently, it did not consider

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[6] *Baird* held only that an investor had a cause of action against an exchange for its failure to enforce compliance by a member with the Act or the exchange's rules under § 6, as it existed prior to the 1975 Amendments. That section provided in relevant part:

> (b) No registation shall be granted or remain in force unless the rules of the exchange include provision for the expulsion, suspension, or disciplining of a member for conduct or proceeding inconsistent with just and equitable principles of trade, and declare that the willful

defendants' second argument. We affirm because Brawer failed adequately to allege fraud or bad faith.

Brawer asks us to reaffirm the private cause of action established in *Baird* for the failure of an exchange to enforce its rules as required by pre-1975 Amendments § 6, and to extend it to include a cause of action for the failure of an exchange to comply with its own rules under §§ 6, 17A, and 19, as amended. However, here the action involved was discretionary. Courts have consistently held that "absent allegations of bad faith [an exchange and its officials] may not be held for discretionary actions taken in the discharge of their duties pursuant to the rules and regulations of the Exchange." *P.J. Taggares Co. v. New York Mercantile Exchange*, 476 F. Supp. 72, 76 (S.D.N.Y. 1979). We recently reaffirmed this view in *Sam Wong & Son, Inc. v. New York Mercantile Exchange*, 735 F.2d 653, 670 (2d Cir. 1984) ("That bad faith is the standard of liability for suits against an exchange with respect to its taking action authorized by applicable law has been established at least since *Daniel v. Board of Trade*, 164

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violation of any provisions of this title or any rule or regulation thereunder shall be considered conduct or proceeding inconsistent with just and equitable principles of trade.

(d) If it appears to the Commission that the exchange applying for registration is so organized as to be able to comply with the provisions of this title and the rules and regulations thereunder and that the rules of the exchange are just and adequate to insure fair dealing and to protect investors, the Commission shall cause such exchange to be registered as a national securities exchange.

The district court noted that in this case no member was involved and that Brawer had only alleged that AMEX and OCC had failed to comply with their own rules. However, it concluded that "[t]he distinction does not appear to be significant to the determination whether there is a private right of action under § 6 against an exchange." 633 F. Supp. at 1257 n.5. We express no opinion as to this conclusion. *See* note 2, *supra*.

F.2d 815 (7th Cir. 1947) . . . ."). That these decisions involved suits under the Commodity Exchange Act, 7 U.S.C. § 1 *et seq.*, makes no difference. The bad faith standard expressly established by Congress for Commodity Exchange Act cases in a 1982 amendment, 7 U.S.C. § 25(b)(4), merely codified existing case law under that statute, 735 F.2d at 676 n.30.[7] Moreover, courts have applied the bad faith standard in suits alleging violations of discretionary rules by the securities exchanges as well. *See, e.g., Schonholtz v. American Stock Exchange, Inc.*, 376 F. Supp. 1089, 1092 (S.D.N.Y.) (dismissing complaint because allegations of exchange rule violations were not coupled with claims of fraud), *aff'd*, 505 F.2d 699 (2d Cir. 1974) (per curiam) and cases cited therein. *But cf. Rich v. New York Stock Exchange*, 522 F.2d 153, 155 n.4 (2d Cir. 1975) (noting that the courts apply a negligence standard to claims that an exchange failed to supervise adequately its members).

There are good reasons why a negligence standard has not been and should not be applied to SRO decision-making.[8] First, applying a negligence standard in such cases would force a court to substitute its judgment for that of the experts on the exchange. *See Aronson v. McCormick*, 13 Misc.2d 1077, 178 N.Y.S.2d 957, 959 (Sup. Ct.), *aff'd mem.*, 6 A.D.2d 999, 177 N.Y.S.2d 1004 (1958). In doing so, a court would be aided neither by specific statutory standards nor by any particular financial

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[7]Although *Sam Wong* was decided after Congress amended the Commodity Exchange Act to include an express bad faith standard, the claim being considered in *Sam Wong* arose before the amendment. The court used the amendment as evidence of what Congress believed that the statute required prior to its amendment. 735 F.2d at 676 n.30.

[8]Here, the relevant by-laws obviously gave AMEX and OCC great discretion. Under a different rule, a different sort of duty might obtain. *See Baird*, 141 F.2d at 244.

expertise, *cf. Auerbach v. Bennett*, 419 N.Y.S.2d 920, 926, 47 N.Y.2d 619, 630 (Ct. App. 1979). Moreover, after-the-fact litigation would be a "most important device" with which to evaluate SRO decisions. *Cf. Joy v. North*, 692 F.2d 880, 886 (2d Cir. 1982), *cert. denied*, 460 U.S. 1051 (1983).

Second, such an intrusion would conflict with the Congressional scheme of exchange self-regulation. As the Supreme Court recognized in *Silver v. New York Stock Exchange*, 373 U.S. 341, 352 (1963), quoting Justice Douglas during his tenure as Chairman of the SEC, the intention of the Act was "one of 'letting the exchanges take the leadership with Government playing a residual role. Government would keep the shotgun, so to speak, behind the door, loaded, well oiled, cleaned, ready for use but with the hope it would never have to be used.'" A negligence standard would bring the government's "shotgun" into almost everyday use.

Third, this governmental intrusion, particularly if it did not employ statutory standards of review, would only serve to increase market uncertainty. Every decision made by a SRO would be subject to litigation and judicial review because "any decision the Committee makes will benefit one group of option investors at the expense of another." 633 F. Supp. at 1261-62. The resulting uncertainty benefits no one. *See, e.g.*, J. Pappas & E. Brigham, *Managerial Economics*, 82-86 (3d ed. 1979). As the SEC pointed out in its amicus brief, "[w]hat is essential in such a situation, for the benefit of all investors, is that the decision be made fairly and considered final."

Brawer's argument that OCC's adjustment rule is not discretionary need not detain us long. Although the rule employs the imperative "shall", it also vests the decision

as to what adjustments should be made "in the sole discretion" of the Securities Committee. OCC and AMEX read the rule as allowing the Securities Committee discretion whether to make any adjustments at all. We agree. *See, e.g., Fogel v. Chestnutt*, 533 F.2d 731, 753 (2d Cir. 1975) ("an exchange has a substantial degree of power to interpret its own rules"), *cert. denied*, 429 U.S. 824 (1976); *Intercontinental Industries, Inc. v. American Stock Exchange*, 452 F.2d 935, 940 (5th Cir. 1971) ("Since these are the rules of the Exchange, it should be allowed broad discretion in the determination of their meaning and application."), *cert. denied*, 409 U.S. 842 (1972).

In his complaint, Brawer alleges that the Securities Committee decided not to adjust because unadjusted options were more efficient as instruments of arbitrage and therefore generate increased trading volumes and revenues. Even if Brawer's claim is true, and OCC and AMEX disagree with the factual premise, he has not made out a sufficient claim of bad faith. As we recently recognized in denying a similar claim of bad faith as too remote and speculative, "[i]f such a degree of self-interest were allowed to demonstrate bad faith, then exchange board members . . . would inevitably be subject to bad-faith charges, and the concept of exchange self-regulation would be undermined." *Sam Wong*, 735 F.2d at 672 (quoting 571 F. Supp. 1530, 1545 (S.D.N.Y. 1983)). Nor do we give any weight to Brawer's argument that bad faith may be found because there was no significant distinction between the first Phillips financing scheme, which apparently would have prompted OCC and AMEX to adjust option prices, and the second financing scheme which resulted in no action by OCC and AMEX. The Securities Committee found that the two financing schemes were

sufficiently different to justify different treatment. We decline to substitute our judgment for theirs.[9]

More troublesome is Brawer's claim that OCC and AMEX sterilized their discretion by waiting over three trading days before meeting to decide whether to adjust. This delay was compounded by the allegation that OCC staff members had been stating as early as Monday, March 4 that no adjustment would be made. Brawer claims that by the time the Securities Committee met, they could make no other decision than not to adjust. However, some of that time was apparently spent marshalling information about the second financing scheme. Without this information the Securities Committee would have been subject to a claim of bad faith for failing to be adequately informed.[10] Thus, we are reluctant to require such a Committee to make a "snap" decision. While the issue is close, we think that the mere failure to hold a meeting until three days after the announcement of the second financing scheme does not, without more, amount to a claim of bad faith.

Affirmed.

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[9]We do not mean to foreclose the possibility that disparate treatment of essentially identical financing schemes might be so arbitrary as to constitute constructive bad faith. However, in this case, Brawer has not alleged a sufficient identity between the two plans to induce us to second-guess the Securities Committee's conclusion.

[10]Indeed, Brawer makes just such a claim in the instant case.

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

- -x

LEONARD BRAWER,

Plaintiff

- against -

THE OPTIONS CLEARING CORPORATION
and AMERICAN STOCK EXCHANGE, INC.,

Defendants.

- -x

85 Civ. 2148 (LLS)

OPINION and ORDER

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LOUIS L. STANTON, D.J.

Defendants The Options Clearing Corporation ("OCC") and American Stock Exchange, Inc. ("AMEX") move pursuant to Fed. R. Civ. P. 12(b) (6) to dismiss the complaint for failure to state a claim upon which relief can be granted, on the ground that there is no private right of action under the applicable provisions of the Securities Exchange Act of 1934 ("Exchange Act" or "Act"), 15 U.S.C. § 78a et seq., under which plaintiff sues; and pursuant to Fed. R. Civ. P. 9(b) for failure to allege fraud or bad faith with the requisite particularity.

Background

The AMEX and OCC are both "self-regulatory organizations" ("SROs") under the Exchange Act, 15 U.S.C. § 78c(a) (26).

The AMEX is registered as a national securities exchange pursuant to § 6 of the Exchange Act, 15 U.S.C. § 78f, and OCC is registered clearing agency pursuant to § 17A of the Act, 15 U.S.C. § 78q-1. Plaintiff is an investor who wrote options on stock issued by Phillips Petroleum Company ("Phillips"). The AMEX provides an exchange market for the trading of options with standard terms, and options on Phillips stock were and are listed and traded at AMEX. All trades in these options are cleared by the OCC.

Plaintiff alleges that at the close of business of March 1, 1985, he held short positions in put options on Phillips stock, under which he was obligated to purchase Phillips stock at the exercise price if the holder of the option required it of him. Between the close of business on March 1, 1985 and the opening of business on March

4, 1985, Phillips, then the target of a hostile takeover, announced a financing scheme or "offer",[1] whereby it would issue a package of debt securities in return for approximately half of its outstanding shares of stock. The Phillips plan was formally announced by a prospectus dated March 4, 1985. While the plaintiff's explanation of the plan's effect upon him is less than clear, it is evident that it caused the price of Phillips stock to fall substantially and thus increased the value of put options and the burdens on plaintiff in meeting his obligations as a writer of puts.

Pursuant to AMEX Rules 902 and 903[2] and OCC By-Laws, Article VI, Section 11 (the "OCC Adjustment Rule"),[3] when a company announces a reorganization that affects its securities, the Securities Committee, consisting of two representatives of each

Exchange of which option contracts in that underlying security are trading and the Chairman of the OCC, shall "make such adjustments in the exercise price . . . as that Committee in its sole discretion determines to be fair" to the holders and writers of option contracts. Upon the announcement by Phillips of its financing plan, defendants' representatives duly met but decided to make no adjustment to the options on Phillips stock.

Plaintiff claims that defendants should have reduced his burdens by an adjustment such as altering his obligation to purchase under the puts he had written, or reducing the exercise price. He alleges that defendants, in failing to adjust option contracts on Phillips stock in response to Phillips's "plan of recapitalization", failed to comply with their own rules and thus violated §§ 6(b), 17A(b) (3) and 19(g)

(1) of the Exchange Act, respectively 15 U.S.C. §§ 78f(b), 78q-1(b) (3) and 78s(g) (1). Although those sections do not expressly grant plaintiff a private right of action against defendants, he argues that such a right of action is implied to allow an injured investor to sue an exchange or clearing agency which fails to comply with its own rules.

Plaintiff relies heavily on Baird v. Franklin, 141 F.2d 238 (2d Cir.), cert. denied, 323 U.S. 737 (1944), in which the Court of Appeals for the Second Circuit held that an investor had a private right of action, under the then § 6(b) of the Act,[4] against an exchange for failure to enforce its rules. In that case the defendant New York Stock Exchange had failed to discipline a member broker firm which converted the plaintiff's securities, in violation of the Act and of the

Exchange's Rules. At that time Section 6(b) provided that the SEC would not register an exchange unless its rules provided for appropriate discipline of its members for conduct "inconsistent with just and equitable principles of trade". Section 6(d) required that the exchange be "so organized as to be able to comply with the provisions of this title and the rules and regulations thereunder and that the rules of the exchange are just and adequate to insure fair dealing and to protect investors". Those sections imposed "the two-fold duty upon an exchange of enacting certain rules and regulations and of seeing that they are enforced." Baird at 244. The court observed that a primary purpose of the Act is the protection of the general investing public, and that for that purpose it was necessary to grant investors "individual causes of action to enforce the

statutory duties imposed upon the exchanges." Id., at 245.

At that time, only two sections of the Act, §§ 19 and 23 (15 U.S.C. §§ 78s, 78ff), explicitly imposed sanctions on an exchange for violations, and they provided for the withdrawal of an exchange's registration and suspending or fining its officers or members. The court found both inadequate to protect the defrauded investor, since they were "punitive and remedial measures, rather than compensatory". Ibid. It held that to construe § 6 as granting no private right of action would defeat the statute's purpose of protecting investors. That the statute itself provided no procedure by which the injured investor could proceed was immaterial, because "[i]t is well established that members of a class for whose protection a statutory duty is created may sue for injuries resulting from

its breach and that the common law will supply a remedy if the statute gives none." Ibid; see Texas & P.R. Co. v. Rigsby, 241 U.S. 33 (1916).

Plaintiff contends that Baird supports the conclusion that the present section 6(b), 17A(b) (3) and 19(g) (1) imply he has a right of action against both defendants for their failure to comply with their rules.[5]

For over 30 years this Circuit and other federal courts followed Baird and recognized an implied right of action against an exchange under than § 6(b). See Arneil v. Ramsey, 550 F.2d 774 (2d Cir. 1977); Lank v. New York Stock Exchange, 548 F.2d 61 (2d Cir. 1977); Rich v. New York Stock Exchange, 522 F.2d 153 (2d Cir. 1975); Rich v. New York Stock Exchange, 509 F. Supp. 87 (S.D.N.Y. 1981); Kroese v. New York Stock Exchange, 227 F. Supp. 519

(S.D.N.Y. 1964); Hughes v. Dempsey-Tegeler & Co., [1973 Transfer Binder] CCH Fed. Sec. L. Rep. ¶ 94, 133 (C.D. Cal. 1974), aff'd, 534 F.2d 156 (9th Cir. 1976), see also Hochfelder v. Midwest Stock Exchange, 503 F.2d 364 (7th Cir.), cert. denied, 419 U.S. 875 (1974) (assumed for purposes of the decision that § 6 created duty in Exchange enforceable in private action, but found no connection between losses and asserted breach of duty, and found in favor of defendant). At least one federal court did not. See Walck v. American Stock Exchange, Inc., 687 F.2d 778 (3rd Cir. 1982); compare, Gustafson v. Strangis, 572 F. Supp. 1154 (D. Minn. 1983) (no private right of action under § 15A against NASD for failure to enforce rules). Significantly, however, every decision in this Circuit following Baird was decided on facts existing prior to the 1975 Amendments

to the Exchange Act. Those Amendments restructured § 6, added new §§ 17A and 19(g), and strengthened the role of the SEC in overseeing the activities of SROs' to ensure that they act in the public interest. See §§ 19(h) and 21(d) and (e). As discussed more fully below, the Amendments end the continuing vitality of Baird.

A second development subsequent to most of the Second Circuit decisions following Baird is a series of Supreme Court decisions setting stricter standards for the implication of private remedies where statutes do not expressly provide them. Thus, although a private damages remedy was held to be implied in former § 6 of the Act, whether one should now be implied from the present statute is a different question.[6]

Discussion

1. The 1975 Amendments

Realizing that the securities industry was faltering under inefficiencies and inadequate regulation and enforcement, Congress amended the Act in 1975. Of significant concern were the SROs' failures to respond appropriately to their statutory obligations. In an effort to preserve their self-regulation yet increase regulatory oversight of SRO activities and function, Congress amended the provisions dealing with SRO's better to define their obligations, see §§ 6, 17A and 19(g), and simultaneously broadened the oversight and enforcement powers of the SEC. Sections 19(h) and 21(d) and (e). Congress

developed comprehensive scheme, contemplating that "self-regulation would be continued, but the SEC would be expected to play a much larger role than it has in the past would be expected to play a much larger role than it has in the past to ensure that there is no gap between self-regulatory performance and regulatory need." Senate Committee on Banking, Housing and Urban Affairs, S. Rep. No. 75, 94th Cong., 1st Sess. 23, reprinted in 1975 U.S. Code Cong. & Ad News 179, 181 ("Senate Report").

In the new section 6(b), Congress for the first time expressly required that an exchange, to be registered, must enforce its own rules. That section directs, in relevant part, that -

> (b) an exchange shall not be registered as national securities exchange unless the Commission determines that --
>
> > (1) Such exchange is so organized and has the capacity to be able to

> carry out the purposes of this chapter and to comply, and (subject to any rule or order of the Commission pursuant to section 78q(d) or 78s (g) (2) of this title) to enforce compliance by its members and persons associated with its member with the provisions of this chapter, the rules and regulations thereunder, and the rules of the exchange.

The 1975 Amendments added § 17A to the Act, thus also providing for the first time for registration and SEC regulation of clearing agencies. That section reads, in relevant part, as follows:

> (3) A clearing agency shall not be registered unless the Commission determines that --
>
> > (A) Such clearing agency is so organized and has the capacity to be able to facilitate the prompt and accurate clearance and settlement of securities transactions for which it is responsible, to safeguard securities and funds in its custody or control or for which it is responsible, to comply with the provisions of this chapter and the rules and regulations thereunder, to enforce (subject to any rule or order of the Commission pursuant to section 78g(d) or 78s(g) (2) of this

> title) compliance by it participants with the rules of the clearing agency, and to carry out the purposes of this section.

The SRO's duty to comply with and enforce compliance with their own rules is found in new § 19(g) (1), which directs that --

> (g) (1) Every self-regulatory organization shall comply with the provisions of this chapter, the rules and regulations thereunder, and its own rules, and (subject to the provisions of section 78q(d) of this title, paragraph (2) of this subsection, and the rules thereunder) absent reasonable justification or excuse enforce compliance --
>
> > (A) in the case of a national securities exchange, with such provisions by its members and persons associated with its members;
> >
> > (B) in the case of a registered securities association, with such provisions and the provisions of the rules of the Municipal Securities Rulemaking Board by its members and persons associated with its members; and
> >
> > (C) in the case of a registered clearing agency, with its own rules by its participants.

While making explicit the duty of a SRO to comply with its own rules, Congress simultaneously vested in the SEC the authority and obligation to enforce that duty. Section 19(h) (1) directs:

> (h) (1) The appropriate regulatory agency for a self-regulatory organization is authorized, by order, if in its opinion such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of this chapter, to suspend for a period not exceeding twelve months or revoke the registration of such self-regulatory organization, or to censure or impose limitations upon the activities, functions, and operations of such self-regulatory organization, if such appropriate regulatory agency finds, on the record after notice and opportunity for hearing, that such self-regulatory organization has violated or is unable to comply with any provision of this chapter, the rules or regulations thereunder, or its own rules excuse has failed to enforce compliance --
>
> > (A) in the case of a national securities exchange, with any such provision by a member thereof or a person associated with a member thereof;
> >
> > (B) in the case of a registered securities association, with any

> such provision or any provision of tne rules of the Municipal Securities Rulemaking Board by a member thereof or a person associated with a member thereof; or
>
> (C) in the case of a registered clearing agency, with any provision of its own rules by a participant therein.

The SEC is "the appropriate regulatory agency" for the AMEX and OCC, 15 U.S.C. § 78c(a) (34). Section 19(h) (1) was added specifically to enforce § 19(g) and to "significantly increase the regulatory options available to [the SEC] to deal with perceived self-regulatory shortcomings." Senate Report, p. 212. The sanctions provided in § 19(h) (1) "are in addition to suspension and deregistration and are intended to provide more usable sanctions that the SEC's traditional 'big stick,'"[7] Ibid.

Moreover, Congress added §§ 21(d) and (e), which empower the SEC to apply to a

federal court for injunctive relief against violations of its rules by an SRO or its members, and to compel an SRO to enforce compliance by its members, when it appears to the SEC that (1) the SRO is unable or unwilling to take appropriate action or (2) such action is necessary in the public interest or for the protection of investors. Section 21(f); see Senate Report, p. 213.

The addition of these expanded and more flexible powers argues that Congress selected the experience and the expertise of the SEC as the preferred source of remedies for an SRO's shortcomings. Rather than codifying Baird, as plaintiff argues, the revisions strengthened the system of self-regulation:

> Although self-regulation has not always performed up to expectations, on the whole it has worked well, and the Committee believes it should be preserved and strengthened. [The Amendments are] designed to accomplish

> this, not only by clarifying regulatory responsibilities at all levels but also assuring that the self-regulatory organizations follow effective and fair procedures, that their activities are not anticompetitive and that the Commission's oversight powers are ample and its responsibility to correct self-regulatory lapses is unmistakable.

Senate Report, p. 201-2

Thus, the concerns expressed in Baird were recognized and addressed by the 1975 Amendments, whose scheme indicates that Congress did not wish to create compensatory sanctions against a SRO for failure to enforce its rules, as it could easily have done, but instead chose remedial measures with enforcement vested in the SEC.

2. Cort v. Ash and New Limitations on Private Rights of Action

Recent Supreme Court decisions reflect a shift in the Court's approach to the

recurring question whether a federal statute implies a private right of action. "As our recent cases -- particularly Cort v. Ash, 422 U.S. 66, 95 S. Ct. 2080, 45 L. Ed.2d 26 -- demonstrate, the fact that a federal statute has been violated and some person harmed does not automatically give rise to a private cause of action in favor of that person." Cannon v. University of Chicago, 441 U.S. 677, 688 (1979); see also Merrill Lynch, Pierce, Fenner & Smith v. Curran, 456 U.S. 353, 377 (1982) (new approach to implication of private remedies requires more careful scrutiny of legislative intent).

A four-factor test determines whether to infer a private remedy. The factors are whether (a) plaintiff is a member of a class for whose special benefit the statute was enacted; (b) there is any indication of legislative intent to create or deny such a

remedy; (c) the implication of the remedy is consistent with the underlying purposes of the legislative scheme and (d) the cause of action is one traditionally relegated to state law. Cort v. Ash, 422 U.S. at 78. The central inquiry is "whether Congress intended to create, either expressly or by implication, a private cause of action." Touche Ross & Co. v. Redington, 442 U.S. 560, 575 (1979); see Transamerica Mortgage Advisors, Inc. v. Lewis, 444 U.S. 11, 15-16 (1979).

(a) Class for whose "especial benefit the statute was enacted"

In determining this factor, the court looks to "the language of the statue itself", Cannon v. University of Chicago, 441 U.S. at 689 (1979). It is clear that both new § 6(b) and § 17A were enacted for

the benefit of investors and the public. Section 6 includes as a prerequisite to the registration of an exchange that its rules "are designed . . . in general, to protect investors and the public interest"; § 6(b)(5); see also § 6(a); Walck v. American Stock Exchange, 687 F.2d at 783. Similarly, § 17A(b)(3) provides that a clearing agency will not be registered unless its rules "are designed . . . in general, to protect investors and the public interest". § 17A(b)(3)(F); see also § 17A(a)(1)(A).

"[T]he mere fact that the statute was designed to protect [investors] does not require the implication of a private cause of action for damages on their behalf . . . The dispositive question remains whether Congress intended to create any such remedy." Transamerica Mortgage Advisors, Inc. v. Lewis, 444 U.S. at 24 (citations

omitted); see also Walck v. American Stock Exchange, Inc., 687 F.2d at 783-84. Supplementing the SEC's enforcement powers, Congress stated that those powers are to be invoked by the SEC when it believes enforcement action is "necessary or appropriate in the public interest" or "for the protection of investors". See §§ 19(h)(1), 19(h)(4) and 21(f). Thus while § 6 and § 17A were indeed enacted for the protection of investors, it is the SEC that will provide that protection.

There is no indication that the statute was enacted to benefit any particular class of investors such as holders or writers of options.

(b) Legislative intent

The second Cort factor looks to the legislative intent. The appropriate

materials to examine are those of the 1975 Amendments. The relevant changes and additions were discussed above, and the concept informing the amendments favors increased supervision and regulation by the SEC, with more sensitive and flexible enforcement capacities, rather than the implication of a private remedy.

None of sections 6, 17A or 19 mention a private remedy Congress provided private remedies under other sections of the Act, §§ 9(e), 16(b) and 18, and "[o]bviously, then, when Congress wished to provide a private damages remedy, it knew how to do so and did so expressly." Touch Ross & Co. v. Redington, 442 U.S. at 572. While the fact that Congress did not expressly so provide here does not foreclose the implication of a private remedy under these sections, see Transamerica v. Lewis, 444 U.S. at 19, the Senate Report shows that

Congress did consider the necessity of improved enforcement and chose to vest that power in the SEC. The Report expresses legislative intent to preserve self-regulation in the industry and to rely on the SEC for enforcement of SROs' performance.

(c) Purpose of the legislative scheme

If an implied remedy would be "necessary or at least helpful to the accomplishment of the statutory purpose", it weighs in favor of implication. Cannon v. University of Chicago, 441 U.S. at 703. Here, to imply a remedy under § 6 would frustrate Congress' purposes.

In Baird, the court found a need for a private right of action because the SEC enforcement powers were not appropriate for protection of the investor. At that time,

and until 1975, a SRO's obligation to comply and enforce compliance with its own rules was not explicit in the statute and the SEC's enforcement powers, to the extent they could be invoked for such purposes, were limited and extreme. See Jennings, "Self-Regulation in the Securities Industry: The Role of the Securities and Exchange Commission", 29 Law and Contemporary Problems 663, 671-2 and 682 (1964); see also Walck v. American Stock Exchange, 687 F.2d at 784-85. That is no longer the case, since Congress has made explicit the duties of the SROs' and vested broad and flexible powers in the SEC to see that those duties are performed and investors are protected.

The nature of the OCC Adjustment Rule is such that the implication of a private cause of action could undermine the ability of the OCC and AMEX to perform their

functions. The rule vests in the Securities Committee, composed of representatives of the AMEX and OCC, broad discretion to determine to what extent adjustment should be made in fairness to all investors when the issuer's unforeseen transaction affects the underlying security. Necessarily, any decision the Committee makes will benefit one group of option investors at the expense of another. Granting such investors private rights of action against such decisions would invite litigation each time the Committee functioned, undermine the self-regulation contemplated by the Act, and remove options adjustment decisions to federal courts rather than the appropriate agencies.

The Preservation Doctrine

Plaintiff argues that under Merrill Lynch v. Curran, 456 U.S. 353 (1982) the private remedy first implied in Baird should be "preserved" since the legislative history of the 1975 Amendments does not indicate otherwise. Curran holds that where "Congress acts in a statutory context in which an implied private remedy has already been recognized by the courts,. . . the question . . . is whether Congress intended to preserve the pre-existing remedy", not whether Congress intended to create a new remedy. Id., at 378-9.

Curran involved an action for damages by an investor in commodity futures contracts against his brokers for violations of a provision of the Commodity Exchange Act ("CEA") and three actions by speculators in futures contracts against

the New York Mercantile Exchange for its failure to enforce its own rules. The CEA was substantially amended in 1974 to create and grant regulatory and enforcement powers to the Commodity Futures Trading Exchange Commission, among other things. The 1974 amendments, like the original legislation, did not mention private remedies for investors injured by a violation of the CEA. The Court found that, since prior to the amendments "federal courts [had] routinely and consistently . . . recognized an implied private cause of action" under the CEA, id., at 379, and the existence of the private remedy was "well understood", id., at 380, Congress had intended to preserve private remedies for investors against exchanges and its participants for violation of the CEA.

That is not the situation here. Although it appears that an implied cause

of action under § 6 was equally "well understood" prior to the 1975 Amendments, but see Hochfelder v. Midwest Stock Exchange, 503 F.2d 364 (7th Cir.), cert. denied, 419 U.S. 875 (1974), several other factors suggest that Congress did not intend to preserve a private right of action under § 6 when it enacted the 1975 Amendments.

In Curran, the Court found specific evidence in the legislative history, suggesting that Congress was aware of and wished to preserve the implied cause of action, intending the new procedures for relief to supplement rather than supplant the judicial remedy. See id., at 382-88. No such evidence appears here regarding the 1975 Amendments, whose intent is rather to centralize enforcement power in the SEC and preserve the system of self-regulation.

In Curran, amidst a "comprehensive reexamination and significant amendment" of the CEA, Congress had left intact the statutory provisions under which the federal courts had implied a cause of action. Id., at 381. This showed that "Congress affirmatively intended to preserve that remedy." Id., at 381-82. That is not so here. Congress did not leave intact, but changed, the sections on which plaintiff relies. Those sections were restructured or added as part of the legislative scheme described above, defining the SROs' obligations and vesting the SEC with enhanced powers to regulate them.

Accordingly, the observations and reasoning in Curran do not lead to the conclusion that Congress intended to preserve a private cause of action under § 6(d) when it amended the Exchange Act.

Conclusion

Accordingly, it is unnecessary to consider the point of pleading raised by the defendants. For plaintiff's lack of private right of action, the complaint is dismissed.

So ordered.

Dated: New York, New York
April 29, 1986

LOUIS L. STANTON
U. S. D. J.

Footnotes

1. Whether Phillip's activities constituted a plan of recapitalization or a tender offer is disputed by the parties; however, the distinction is not material to this motion.

2. The relevant parts of AMEX Rules 902 and 903 read as follows:

   902(a) Subject to the provisions of Rules 905, 907 and 909, the rights and obligations of holders and writers of option contracts of any class of options dealt in on the Exchange shall be as set forth in the rules of the Options Clearing Corporation.

   903(c) The unit of trading and the exercise price initially established for option contracts of a particular series are subject to adjustment in accordance with the rules of the Options Clearing Corporation. When such adjustment or adjustments have been determined, announcement thereof shall be made by the Exchange and, effective as of the time specified in such announcement, the adjusted unit of trading and the adjusted exercise price shall be applicable with respect to all subsequent transactions in such series of options.

(d) Option contracts shall be subject to adjustments in accordance with the rules of the Options Clearing Corporation.

3. The OCC Adjustment Rule reads in pertinent part as follows:

> SECTION 11. Whenever there is declared a . . . reorganization, recapitalization or reclassification or similar event in respect of any underlying security, the number of outstanding option contracts, the unit of trading and/or the exercise price with respect to all option contracts open for trading in that underlying security shall be adjusted, effective on the "ex-date" of the underlying security in the primary market, in accordance with this Section 11. . . .
>
> (d) In the case of any reorganization, recapitalization, reclassification, or similar event with respect to shares of underlying securities for which adjustment is not provided in any of the foregoing paragraphs of this Section 11, or in the case of any event for which adjustment is provided in one of the foregoing paragraphs but is not considered by the Securities Committee to be appropriate under the circumstances, the Securities Committee shall make such adjustments in the exercise price, trading unit or number of

contracts with respect to the option contracts affected by such event as that Committee in its sole discretion determines to be fair to the holders and writers of such option contracts.

(e) The Securities Committee, in exercising its functions pursuant to paragraphs (c) or (d) of this Section 11 regarding adjustment or option contracts in an underlying security, shall consist of two designated representatives of each Exchange on which option contracts in that underlying security are open for trading and the Chairman of [OCC]. The vote of a majority of the voting members of the Securities Committee shall constitute the action of the Committee. The Chairman of [OCC] shall not be a voting member of the Committee except in the case of a tie vote, in which case the Chairman shall have the right to case a vote to break the tie and shall, for such purpose, be deemed to be a voting member. The members of the Securities Committee need not be Clearing Members or officers or directors of [OCC]. The Securities Committee may transact its business by telephone.

4. Old § 6 provided, in relevant part:

(b) "No registration shall be granted or remain in force unless the rules of the exchange include provision for the expulsion, suspension, or disciplining of a member for conduct or proceeding inconsistent with just and equitable principles of trade, and declare that the willful violation of any provisions of this title or any rule or regulation thereunder shall be considered conduct or proceeding inconsistent with just and equitable principles of trade."

(d) "If it appears to the Commission that the exchange applying for registration is so organized as to be able to comply with the provision of this title and the rules and regulations thereunder that the rules of the exchange are just and adequate to insure fair dealing and to protect investors, the Commission shall cause such exchange to be registered as a national securities exchange."

5. In Baird, the Exchange failed to enforce compliance by a member with the Act and the Exchange's rules. In this action, no member is involved; the Exchange and OCC failed to comply with their own rules. The distinction does not appear to be significant to the determination whether there is a private right of action under § 6 against an exchange. See Bright v. Philadelphia-Baltimore-Washington Stock

Exchange, 327 F. Supp. 495 (E.D. Penn. 1971); cf. New York Stock Exchange, Inc. v. Sloan, 394 F. Supp. 1303 (S.D.N.Y. 1975).

6. The district courts in this Circuit, as well as other federal courts, are similarly reconsidering whether there is an implied remedy under § 6 against a broker-dealer for its violation of an exchange's rules. See Picard v. Wall St. Discount Corp., 526 F. Supp. 1248 (S.D.N.Y. 1981); Jablon v. Dean Witter & Co., 614 F.2d 677 (9th Cir. 1980). The Court of Appeals for the Second Circuit had first implied such a remedy in Colonial Realty Co. v. Bach & Co., 358 F.2d 178 (2d Cir.), cert. denied, 385 U.S. 817 (1966), which held that a private cause of action may exist under § 6 of the Securities Act for violations of some N.Y.S.E. Rules. However, in light of the Supreme Court's new standards for implying remedies, as set forth in Cort v. Ash, 422 U.S. 66 (1975) and subsequent cases, federal courts are re-evaluating whether such a right should be implied and finding that it should not. Picard v. Wall St. Discount Corp., 526 F. Supp. at 1251.

7. In addition to these enforcement powers, the SEC can abrogate or amend any SRO's rules. § 19(c). A SRO must file for approval with the SEC a copy of any proposed rule or rule change, accompanied by a statement with reasons for the proposal. § 19(b). Moreover, the SEC has authority to prescribe rules regulating the activities of clearing agencies if it is necessary in the public interest, to protect

investors or in furtherance of the principles of the statute. § 17A (d) (1).

UNITED STATES COURT OF APPEALS
FOR THE
SECOND CIRCUIT

At a stated Term of the United States Court of Appeals for the Second Circuit, held at the United States Courthouse in the City of New York, on the 11th day of December one thousand nine hundred and eighty-six.

Present: HON. J. EDWARD LUMBARD

HON. RICHARD J. CARDAMONE,

HON. LAWRENCE W. PIERCE,

Circuit Judges,

LEONARD BRAWER,

Plaintiff-Appellant,

v.

THE OPTIONS CLEARING CORP AND AMERICAN STOCK EXCHANGE, INC.,

Defendants-Appellees.

No. 86-7416

Appeal from the United States District Court of the Southern District of New York.

This cause came on to be heard on the transcript of record from the United States District Court for the Southern District of New York, and was argued by counsel.

ON CONSIDERATION WHEREOF, it is now hereby ordered adjudged and decreed that the JUDGEMENT of said District Court be and it hereby is AFFIRMED in accordance with the opinion of this Court with costs to be taxed against the appellant.

ELAINE B. GOLDSMITH,
CLERK

EDWARD J. GUARDARO,
DEPUTY CLERK

A-56

UNITED STATES COURT OF APPEAL
FOR THE SECOND CIRCUIT

BRAWER
v.
OPTIONS CLEARING CORP.

NOTICE OF MOTION

state type of motion

for extention of time and leave to file the motion out of time

Brief statement of relief requested:

Extension of time to file petition for rehearing with suggestion for rehearing in banc.

By: (Signature of attorney)

Signed name must be printed beneath

A. Arnold Gershon

Appearing for: (Name of party)

Brawer — Appellant for Petitioner: Plaintiff

Date

December 31, 1986

IT IS HEREBY ORDERED that the motion be and it hereby is granted.

UNITED STATES COURT OF APPEALS
FOR THE
SECOND CIRCUIT

At a stated Term of the United States Court of Appeals, for the Second Circuit, held at the United States Courthouse in the City of New York, on the eleventh day of February one thousand nine hundred and eighty-seven.

LEONARD BRAWER,
Plaintiff-Appellant,

-against-

THE OPTIONS CLEARING CORPORATION and AMERICAN STOCK EXCHANGE, INC.,
Defendants-Appellees.

No. 86-7416

A petition for rehearing containing a suggestion that the action be reheard in banc having been filed herein by counsel for the plaintiff-appellant, Leonard Brawer,

Upon consideration by the panel that heard the appeal, it is

ORDERED that said petition for rehearing is DENIED.

It is further noted that the suggestion for rehearing in banc has been transmitted to the judges of the court in regular active service and to any other judge on the panel that heard the appeal and that no such judge has requested that a vote be taken thereon.

Elaine B. Goldsmith,
Clerk